STATE OF MICHIGAN

COURT OF CLAIMS

REHMANN ROBSON & CO., P.C., Plaintiff,	**OPINION AND ORDER**
v	Case No. 12-000098-MT
DEPARTMENT OF TREASURY, Defendant.	Hon. Michael J. Talbot

This use tax dispute comes before the Court on plaintiff Rehmann Robson & Co., P.C.'s (Rehmann's) motion for summary disposition under MCR 2.116(C)(10). The motion is GRANTED.

STATEMENT OF THE FACTS AND PROCEEDINGS

Rehmann is a large accounting firm headquartered in Saginaw, Michigan. Through its offices located throughout the Midwest, Rehmann provides tax and auditing services to a wide variety of clients. In order to provide these services, Rehmann subscribes to an online information database, *Checkpoint*. At various points throughout the audit period, *Checkpoint* was offered by either Bureau of National Affairs (BNA) or Thomson Reuters. Through *Checkpoint*, Rehmann's professionals research and obtain access to international, state and local, and federal tax materials. Access is obtained by locating *Checkpoint*'s main website through a web browser and inputting a user name and password. No special *Checkpoint* software is downloaded by Rehmann employees to access the database.

Pursuant to an audit conducted of Rehmann's business for the tax periods January 1, 2006 through December 31, 2009, the Department assessed Rehmann use tax under the Michigan Use Tax Act (UTA), MCL 205.91, *et seq.* The assessment was based on the Department's determination that Rehmann's use of *Checkpoint* constituted the sale of tangible personal property in the form of "prewritten computer software."

Paying $55,000 under protest, Rehmann now seeks a refund for use taxes it claims were improperly assessed. Rehmann argues that the transactions upon which the assessed taxes are based were services that did not involve delivery or use of tangible personal property, and are therefore not subject to use tax under the UTA. In the alternative, it asserts that if tangible personal property was delivered in connection with the services, the transfer was merely incidental to the services received, and therefore use tax does not apply. The Department argues that use of *Checkpoint* is taxable as prewritten computer software under the UTA because software is licensed for access and use by Rehmann. It claims that because *Checkpoint* runs by the delivery to the customer's computer of "source" codes that are temporarily transmitted to a customer's web browser when a search is conducted, the transfer or access to these codes constitutes delivery and use of tangible personal property (i.e., prewritten computer software). The Department also contends that the transactions with *Checkpoint* were not "services," and therefore an analysis of whether software was merely incidental to services rendered does not apply.

STANDARD FOR GRANTING SUMMARY DISPOSITION UNDER MCR 2.116(C)(10)

A motion for summary disposition under MCR 2.116(C)(10) is properly granted if no genuine factual dispute exists, and the moving party is entitled to judgment as a matter of law.

Rice v Auto Club Ins Ass 'n, 252 Mich App 25, 31; 651 NW2d 188 (2002). In deciding a motion brought under MCR 2.116(C)(10), a court considers all the evidence, affidavits, pleadings, and admissions in the light most favorable to the nonmoving party. *Id.* at 30-31.

In this case, the parties' disagreement concerns a matter of interpreting the provisions of the UTA. When interpreting a statute, the primary goal "is to give effect to the Legislature's intent, focusing first on the statute' s plain language." *Malpass v Dep 't of Treasury*, 494 Mich 237, 247-248; 833 NW2d 272 (2013). When the words of a statute are unambiguous, the provision s must be enforced as written, and no further judicial construction is permitted. *Id.* at 249.

ISSUES AND ANALYSIS

The issue in this case is whether Rehmann's subscription to *Checkpoint* is properly subject to use tax. Under the UTA, a 6% tax is levied "for the privilege of using, storing, or consuming tangible personal property in this state . . . ." MCL 205.93(1). Resolution of this issue requires a consideration of (1) whether the transactions in question involved the sale of "tangible personal property" as defined under the UTA; (2) whether tangible personal property was "used" by Rehmann within the meaning of the UTA; and (3) if "tangible personal property" was "used" by Rehmann, in connection with the subject transactions, whether use of the tangible personal property was merely incidental under the "incidental to services" test set forth in *Catalina Mktg Sales Corp v Dep't of Treasury*, 470 Mich 13; 678 NW2d 619 (2004).

I. WAS THE SOFTWARE INVOLVED IN THE *CHECKPOINT* TRANSACTIONS "TANGIBLE PERSONAL PROPERTY" WITHIN THE MEANING OF THE UTA?

"Tangible personal property" includes "prewritten computer software," which is defined as "computer software, including prewritten upgrades, that is delivered by any means and that is not designed and developed by the author or other creator to the specifications of a specific purchaser." MCL 205 .92b(o). Thus, for computer software to constitute tangible personal property, it must be "delivered by any means."

"[D]elivered by any means" is not defined in the statute. Unless defined in the statute, every word or phrase of a statute should be accorded its plain and ordinary meaning, considering the context in which the words are used. MCL 8.3a; *Krohn v Home-Owners Ins Co*, 490 Mich 145, 156; 802 NW2d 281 (2011). Dictionary definitions may be consulted to give words their common and ordinary meaning. *Id.* The most relevant, conventional meaning of the word "deliver," given the context of MCL 205.92b(o), is "to take and handover to or leave to another: CONVEY; to hand over, surrender." *Merriam-Webster's Collegiate Dictionary* (2003). Similarly, *Black's Law Dictionary* (9th ed) defines "delivery" as: "[t]he formal act of transferring something; the giving or yielding possession or control of something to another."

The definition of "prewritten computer software" indicates that the UTA applies only to those transactions in which the person takes "delivery" of the software. There is no evidence in the record that Rehmann took "delivery" of prewritten computer software from BNA or Thomason Reuters.[1] The software used to produce the results that Rehmann obtained from *Checkpoint* was not handed over, left, or transferred. BNA and Thomson Reuters, through

[1] The Court finds unpersuasive the Department's assertion that the *de minimus,* temporary transfer of a computer code unto a customer's web browser during a *Checkpoint* search equated to the "delivery" of prewritten computer software.

Checkpoint, did not surrender possession and control of software to Rehmann, or actually transfer the software needed to process and produce the outcomes (i.e., the research results) for which the parties contracted. What was transferred was tax and audit information that had been processed using BNA and Thomson Reuter's own software, hardware, and infrastructure. But the software itself was not "delivered" to Rehmann as that word is commonly used.

In summary, the transactions did not involve "computer software . . . that is delivered by any means . . ." as is necessary to meet the definition of "prewritten computer software," which is "tangible personal property" under the UTA.

II. DID REHMANN "USE" THE PREWRITTEN COMPUTER SOFTWARE WITHIN THE MEANING OF THE UTA?

Even if the Court had concluded that prewritten computer software was "delivered" to Rehmann, the requisite "use" of the software was not made in this case.

The statute defines "use" as "the exercise of a right or power over tangible personal property incident to the ownership of that property including transfer of the property in a transaction where possession is given." MCL 205.92(b). For purposes of the UTA, "use" does not require the transfer of actual possession, but necessitates the exercise of a right or power over the property "incident to ownership." *NACG Leasing v Dep't of Treasury*, 495 Mich 26, 843 NW2d 891 (2014).

The definition of the term "incident to ownership of tangible personal property" is not found in the UTA, nor is there any controlling Michigan case directly on point. However, most Michigan courts that have considered the issue have required a requisite level of control by the

taxpayer before there is deemed to be an incident of ownership for use tax purposes. For example, in *WPGP1, Inc v Dep't of Treasury*, 240 Mich App 414, 612 NW2d 432 (2000), the Court of Appeals considered the many indicators of control over an airplane that the taxpayer leased to a third party. In concluding that the taxpayer did not engage in a taxable use of the airplane in Michigan because it had ceded control of the airplane to the third party, the Court focused on the fact that the third party–and not the taxpayer—completely controlled the flight schedules and the routine maintenance of the airplanes, and that the third party was responsible for ensuring that the aircraft remained duly registered with the Federal Aviation Administration. See also *Fisher & Co, Inc v Dep't of Treasury*, 282 Mich App 207, 212; 769 NW2d 740 (2009) ("The right to control what happens—in layman's terms—to one's property is one of the most fundamental rights incident to ownership," citing *Twichel v MIC Gen Ins Corp*, 469 Mich 524, 534-535; 676 NW2d 616 (2004)). Although the facts in these cases are distinguishable from those in this case, it is clear that "right or power" under the definition of use requires that the taxpayer have some level of control over the tangible personal property before use tax can be properly applied. The record is devoid of any evidence that Rehmann had such control. The only evidence of control by Rehmann was the ability to control research outcomes by inputting certain research terms to be analyzed.

This Court disagrees with the Department's argument that mere "access" to *Checkpoint*'s computer servers equates with "use." Although computer software was involved in most of the transactions in question, there is no evidence in the record that Rehmann exercised a right or power incident to ownership in *Checkpoint*'s underlying software. At the most, Rehmann accessed *Checkpoint*'s computer power and controlled the output of research information by

entering research terms. But Rehmann had no control over the underlying software that may have been used by *Checkpoint* to complete the necessary tasks.

III. WAS REHMANN'S USE OF PREWRITTEN COMPUTER SOFTWARE INCIDENTAL TO THE SERVICES PROVIDED?

Finally, even if prewritten computer software was somehow delivered and used by Rehmann within the meaning of the UTA, any such use was merely incidental to the services rendered through *Checkpoint*, and would not subject the overall transactions to use tax.

In *Catalina*, the Supreme Court adopted the "incidental to services" test articulated in *Univ of Mich Bd of Regents v Dep't of Treasury,* 217 Mich App 665, 553 NW2d 349 (1996), to determine whether a business transaction that involves both the provision of services and the transfer of tangible personal property is a service or a tangible property transaction. Under the "incidental to services" test, a court must look objectively "at the entire transaction to determine whether the transaction is principally a transfer of tangible personal property or a provision of a service." *Catalina*, 470 Mich at 24. The *Catalina* Court identified six factors to consider when making this determination.

The first *Catalina* factor concerns what the buyer sought as the object of the transactions. The license agreements in the record, along with affidavits provided by Rehmann, make it clear the primary objective for entering into the transactions was to access *Checkpoint*'s information services and databases. The Department has presented no persuasive evidence that Rehmann owned or otherwise had title to or responsibility for prewritten computer software provided by *Checkpoint*. Even if the Court were to accept the Department's claim that tangible personal property in the form of source codes was transferred to Rehmann's web browsers when using

Checkpoint, such transfer was momentary and incidental to Rehamnn's primary objective of obtaining information services.

Second, *Catalina* permits the Court to consider what the companies providing *Checkpoint* were in the business of doing. While it is true that both BNA and Thomson Reuters sell books and CDs, they are not in the business of selling prewritten computer software. What was offered was the provision of information services that rendered tax and audit research results in the form of, for example, editorial reports, tax laws, and accounting standards.

Third, under *Catalina,* the Court may consider whether the "goods" (i.e., prewritten computer software) were provided as a retail enterprise with a profit-making motive. The evidence shows that BNA and Thomson Reuter's motives were not to profit from the sale of prewritten computer software, but to profit from the provision of online information services. The Department has not provided any persuasive evidence to the contrary.

Fourth, the Court, under *Catalina*, may properly consider whether the tangible goods (i.e., the prewritten computer software involved in these transactions) were available for sale without the associated services. The record is devoid of any evidence that the software used in obtaining online research results could be purchased separately apart from *Checkpoint*'s information services. As conceded by the Department, the software used in *Checkpoint* could not be "unbundled" separately from the service provided.

The fifth *Catalina* factor looks to the extent to which the intangible services contributed to the value of *Checkpoint*. Any value of *Checkpoint* to Rehmann was directly related to the access to *Checkpoint*'s computer power and database, and the information services provided. No *Checkpoint* software was ever loaded onto Rehmann's computers, and any access to

Checkpoint's software was a conduit to the acquisition of what Rehmann really wanted and contracted for: research results that flowed from *Checkpoint*'s computer power capabilities.

In light of the sixth *Catalina* factor, which permits consideration of any other factors relevant to this transaction, the Court further observes that the Department's characterization of the transactions in question fails to recognize the complexity associated with the computer environment within which Rehmann and businesses around the country are now operating. With the evolution of "on-demand" access to third party providers' networks, servers, and application software, businesses no longer need to install, download, or transfer software—or much of anything—to a computer. Simply put, the technology, as it stands today, allows for access to another's computer power with little to no transfer of tangible personal property, including software. The online interactions between Rehmann and *Checkpoint* are illustrations of the changing nature of computer-based technology and business models that are in essence services with incidental transfers of tangible personal property, or no transfers of tangible personal property at all.

These factors, considered together, leads to the conclusion that prewritten computer software was simply an incidental component of the principal transactions for the information services that Rehmann and *Checkpoint* entered into. In the transactions at issue, Rehmann sought out a service, not software. Further, the companies that provided *Checkpoint* were in the business of providing services, not selling or licensing software. The underlying software used to provide the services were generally not available to customers without the service, and the value of that software was incidental to the services offered alongside it. Any prewritten computer software used in these transactions was incidental to the transactions as a whole.

In light of this ruling, the Court declines to address Rehmann's other arguments, including the argument that the UTA must be interpreted consistent with the Streamlined Sales and Use Tax Act.

CONCLUSION

Rehmann's transactions in question are not subject to Michigan use tax. The transactions here are properly characterized as non-taxable services rendered to Rehmann through an online information service. Unless and until the Legislature expresses an intent to specifically tax transactions involving the remote access to a third party provider's technology infrastructure, transactions such as those described in this case do not fit under the plain meaning of the UTA and are not properly subject to use tax.

IT IS HEREBY ORDERED Rehmann's motion for summary disposition is GRANTED pursuant to MCR 2.116(C)(10). The Court orders the parties to submit a proposed final order conforming to this opinion within 14 days of entry of this opinion.

Dated: NOV 2 6 2014

Hon. Michael J. Talbot
Chief Judge of the Court of Claims